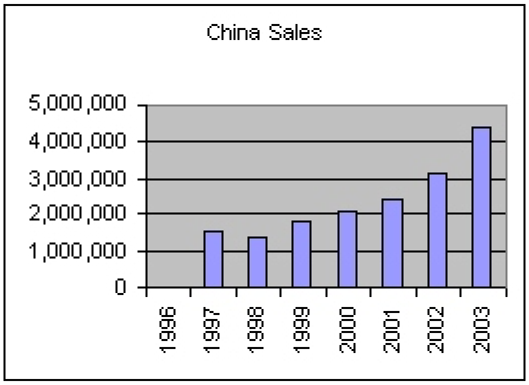
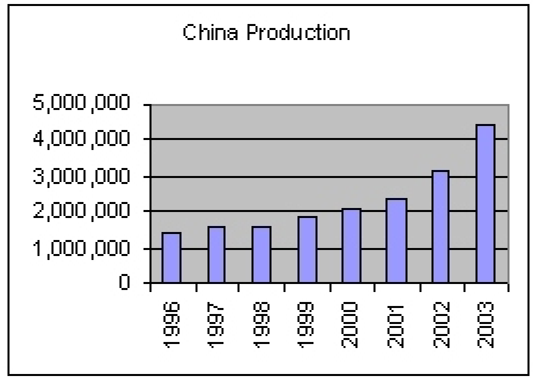
China





Imports/Exports

Total U.S. exports to China in actual U.S. dollars and units

Type	2000	2001	2002	2003
Passenger	$9,837,432	$11,582,427	$26,846,641	57,522,389
Passenger-UNITS	622	455	1,440	2,573
Medium & Heavy Trucks and Tractors	$5,295,632	$3,235,980	$2,048,302	8,817,318
Medium & Heavy Trucks and Tractors-UNITS	73	143	70	151

*Data Source: U.S. Department of Commerce, the U.S. Treasury, and the U.S. International Trade Commission

U.S. General Imports from China in actual dollars and units

List of Commodities	2000	2001	2002	2003
Passenger Vehicles & Light Trucks-DOLLARS	$1,525,774	$3,047,080	$7,826,444	$18,881,344
Passenger Vehicles & Light Trucks-UNITS	1,358	2,774	7,127	24,758

*Data Source: U.S. Department of Commerce, the U.S. Treasury, and the U.S. International Trade Commission

Overview

China is in an explosive stage of development of its auto sector. In the past year, 2003, China produced 4.44 million autos and sold 4.39 million, a yearly rise of 35.2 percent and 34.21 percent respectively. This year, China's automobile production and sales figures are both expected to exceed 5 million units, up about 20 percent year-on- year. This is in sharp contrast to 1992 when China produced 1 million vehicles. The Chinese central government predicts that by 2010, Chinese production will reach 8 million units and 11 million units by 2015.

Over 100 local and foreign automakers are fighting for a piece of the hottest auto market in the world. In a rush to satisfy demand, automakers are increasing manufacturing capacities, cutting prices largely because of reduced tariff barriers resulting from China's accession to the WTO. It is estimated that $18 billion has been invested in auto manufacturing in China since 1994, with $6.3 billion (of the total $18 billion) invested since the beginning of 2002. In comparison, it is estimated that there was $6.1 billion invested in the U.S. auto manufacturing in the same period.

On paper China's auto boom seems unlikely. China has a per capita income of $966 and widespread poverty. Car ownership in China is still only between 5-6 units per 1,000 people. However, China has pockets of wealth and prosperity within its 1.3 billion population.

Due to a lack of real competition, in the early years, market leaders Volkswagen and General Motors were able to charge premium prices in China. After years of building its Chinese and Asian business, General Motor's investment is paying off and making a healthy profit in its Asian operations. For the third quarter of 2003, General Motors reported earnings of US$162 million in its Asian operations, or about US$ 1,200 profit per vehicle sold. This can be compared with North American earnings of US$128 million, or US$102 per vehicle sold. Similarly, Volkswagen reported that 80 percent of its first half 2003 earnings came from China. The thirty percent or more price premiums once charged are disappearing due to increased domestic competition, decreasing tariffs, increasing imports.

Ford, a relative newcomer to the Chinese market, has ambitious plans to become one of the top three vehicle producers in China within the next 5 to 10 years. Ford's current capacity of 20,000 units will be increased to 150,000 units. Ford announced that it will invest an additional U.S.$1.5 billion in manufacturing capacity, new models and expansion of its sales network.

Given the current rush to expand manufacturing capacity in China, there is a growing concern of too much capacity. There are varying views on Chinese manufacturing overcapacity. Estimates range between 1 million units to 2.5 million units excess over sales in the near term. The threat of overcapacity in China causes a concern that unsold cars will be exported, following in the export patterns of Japan and now Korea. Passenger car exports are new for Chinese domestic automakers. Low and medium-end trucks, buses currently account for the majority of China's overseas vehicle exports. Of interest, is the fact that nearly half of the current capacity is from plants with foreign partners.

Large scale exports are not expected within the next five years because the manufacturers are still focusing on building products for the booming domestic car market. In addition, the quality and costs of Chinese products are still not internationally competitive in the near term. It is estimated that China's production costs are 20 to 30 percent higher than in the rest of the world. In the longer term, however, mounting competition, lower manufacturing costs, increased quality and slowing growth of the domestic market may mean Chinese auto exports are inevitable.

As the world's auto manufactures are increasing production in China, Chinese manufacturers are planning to export from China and built plants overseas. It is reported that Chinese car manufacturer, Chery, is negotiating with companies from Venezuela and Pakistan to build plants in those countries. According to a company spokesperson, foreign partners will build plants and buy manufacturing equipment, and Chery will export its engines and spare parts to Venezuela and Pakistan for car production. In addition, Chery will start to produce its own branded cars in June 2004 at a plant in Iran with local partner SKT. Initial annual capacity of 30,000 units is planned in Iran. This will make Chery, the first Chinese automaker to produce passenger cars abroad. Chery also plans to export 10,000 completed cars to Middle East and Central and South America this year, up from 1,000 units last year. Domestically, Chery has set a sales target of 180,000 to 200,000 cars this year. The company has annual domestic production capacity of 350,000 units.

Honda is currently building a plant used to manufacture cars solely for export. Honda is planning to export a small car to Asian markets. Capacity is planned to be 50,000 units. Production is scheduled to begin by the second half of 2004.

Imports and Exports

China's automotive imports increased 84% to $US 14.45 billion in 2003. Complete vehicle imports reached 125,129 units and the value jumped 63% to 5.25 billion US dollars. The value of key components increased 131.9 percent to $US 3 billion, while the value of other auto parts and accessories increased 85% to $US6.2 billion.

Similarly, Chinese exports of automotive products increased 34% to $US 4.71 billion in 2003. Complete vehicle exports reached $US 400 million. Of the 125,000 complete vehicle exported, 2,849 were sedans, 648 cross-country vehicles, 4,224 station wagons, 2,550 large an medium sized buses, 25, 348 heavy-duty trucks and 88,642 special-purpose vehicles. Exports of key components reached $US 630 million, while other parts increased to 3.68 billion dollars.

U.S. passenger vehicle exports to China increased over 70% in 2003 to 2,246 units, or nearly $US 50 million. Similarly, road motor vehicles and medium and heavy duty trucks exports were 1,539 units and 131 units in 2003, increases of 255% and 424% respectively.

Trade Tensions

In November 2003, the Chinese government gave General Motors, Ford and DaimlerChrysler licenses to import about 30,000 vehicles to China through 2005. In addition, the Big Three will be permitted to distribute the cars without having to go through a Chinese company, as is now required. In the past, Chinese trading companies applied for import licenses and decided how to distribute the cars. European and Asian automakers, which account for most vehicle imports in

China, have never been given import licenses or the right to distribute cars. They have always had to use a Chinese trading company. Asian and European companies fear that the Big Three imports could result in allocations being cut for them.

Under this agreement, it is reported that Ford Motor Co. will send 5,250 vehicles to China in the next two calendar years. GM will export about $1.3 billion worth of vehicles and component kits for assembly at its Shanghai-GM partnership, totaling about 20,000 vehicles. They will include a large number of Cadillacs as GM tries to build its luxury brand in China. GM plans to export 4,500 completely built Cadillacs and Buicks. DaimlerChrysler will ship 4,500 U.S.-built vehicles, including Mercedes-Benz M-class SUVs built in its Vance, Ala., plant.

China's decision to give the Big Three import licenses was widely seen as an effort to quiet U.S. lawmakers and industry angry over China's growing trade surplus with the United States.

Chinese Sourcing

General Motors plans to increase by a factor of 20 the number of auto parts it buys from China to use in its manufacturing facilities around the world. In 2003, GM bought about $200 million in Chinese auto parts for use in the rest of the world. It projects to increase purchases from China to grow to $4 billion by 2009. Currently, GM brings more auto parts into China than it exports, but that will change rapidly during the next few years.

GM has announced that it will more than double the number of parts it buys in China for cars it makes in China, from $2.8 billion to $6 billion annually. This is attributable in part to US suppliers establishing manufacturing operations in China because of China's lower wages, lower energy costs, sparse environmental regulations and the currency advantages of making a product in China and shipping it to the United States.

Ford has doubled its purchases from what it calls "low-cost countries" like China, India and South Korea. The number grew from less than $500 million a year to about $1 billion in 2003. Currently, Ford spends about $70 billion a year on parts and materials, including $50 billion from domestic sources.

DaimlerChrysler while not specific, said that it plans to buy more auto parts from China. DaimlerChysler indicated that their purchases in China will grow to a level similar to other worldwide auto manufacturers.

U.S. automakers claim that intense price competition that is pushing them to source and build more products in low cost countries like China.

World Trade Organization

When China formally joined the World Trade Organization (WTO) on December 11, 2001, China committed to numerous market opening measures in the automotive sector of its economy. The gradual elimination of trade barriers to foreign competition as a result of WTO membership is a major force in the transformation of China into a competitive auto producer and consumer. Chinese Government policies have encouraged foreign carmakers to speed up investment and localized production instead of aggressively exporting vehicles to the country. However, China has had varying degrees of success in implementing its WTO commitments.

China has lowered its tariffs on autos. Currently tariffs on imported vehicles are 37.6 percent. By 2006, tariffs on complete vehicles will be 25 % and imported parts will have tariffs of 10.5 % or less.

After a lengthy delay, the Peoples Bank of China issued Auto Finance Regulations which permits auto manufacturers to finance consumer purchases. Recently, the China Banking Regulatory Commission (CBRC) gave permission to GM, Volkswagen and Toyota to establish auto financing companies in China. The SAIC GM Automobile Finance Company, Ltd, Toyota Motor Finance (China) Co. Ltd., and Volkswagen Automobile Finance (China) Co., Ltd. are expected to be set up the early part of 2004, but still need approval to begin offering auto financing services in China. The three companies must submit a report on their equity capital, management, company development plans and other necessary documents within six months. Once they meet CBRC's requirements, they may begin to offer financial services.

The approval of the three foreign auto finance companies mean that Chinese consumers will be able to use loans from traditional non-banking institutions to finance their new car purchases. Currently more than 80 percent of the car buyers still pay cash, while less than 20 percent use loans. The reverse is true in the developed world markets.

Currently, Chinese car customers can only get a car loan from local banks, which began offering them five years ago. The present auto finance service industry has been plagued by bad loans, customers who won't or can't pay back and the lack of credit ratings. In addition, China also has a cultural aversion to debt.

While China has lowered its tariffs and issued finance regulations as it agreed, there are several WTO commitments that China has not successfully implemented. The U.S. automotive industry has several issues that they have encountered since China began implementing its WTO commitments and proposed new Auto Policy. These issues include: an overall lack of transparency in the implementation of its auto commitments, specifically the auto quota, automotive standards regulations, trading and distribution rights.

Interested parties have been taking a low key approach to China's fulfillment of it's major market access commitments, largely because automakers are not pushing the issues for fear that a confrontation would jeopardize existing commercial ties with Chinese government and industry.

A key area of confusion is the import auto quota system for imported vehicles. According to promises upon China's entry into the World Trade Organization, China should end the period for protection of the domestic car industry by the end of 2004. The quota started at $6 US billion and is currently set at $US 10.549 billion. It is scheduled to expire in January 2005. Vice Minister of Commerce Wei Jianguo, confirmed, on February 13, 2004, that China will cancel its auto import quota beginning Jan. 1, 2005. There have never been clear guidelines as to how the quota is allocated among foreign automakers. In addition there has been no information on the amount of the quota used. There has been much confusion concerning quota application due to a general lack of transparency

The US automotive sector has expressed concerns about new standards regulations, and their impact on auto trade. It is argued that the Chinese government is picking and choosing different regulations from around the world and modifying them for use in China. These include both EU and US standards and unique China specific standards. Automakers have argued that the Chinese approach is at odds with global harmonization of the world's existing standards and certification systems, which is taking place at the United Nation's Working Party 29.

China has not yet issued any regulations effecting its WTO accession agreement commitments covering the areas of trading rights and distribution. These two areas should have been fully opened to joint ventures with minority foreign ownership by December 11, 2002, and to all by the end of 2004. This applies not just to autos or auto products, but all goods.

China has traditionally restricted the number of companies with trading rights, the right to import and export goods, and it made extensive use of state trading enterprises. It also restricted the products that a particular company could import or export. In its accession agreement, China agreed to phase in full trading rights over a three-year period. All enterprises in China and all foreign enterprises and individuals were granted full trading rights within three years after accession. China is also reportedly considering a requirement that separate distribution channels be used for domestic and imported autos.

Prior to its WTO accession, China generally did not permit foreign companies to distribute products in China, to provide wholesaling, retailing, franchising or commission agent services or to provide related services, such as repair and maintenance services. In its accession agreement, China agreed to phase out these prohibitions over three years, subject to limited exceptions. To date, China has not issued any of the regulations necessary to implement these commitments.

Proposed China Auto Policy

China is preparing the release of its 10th Five-Year Plan for the Development of the Automobile Industry (China Auto Policy). In the plan, the Chinese government charts the course it intends the industry to follow. The plan covers every aspect of the automobile industry. Implementation of many of China's WTO commitments are outlined in this plan. However, its release and implementation has been significantly delayed.

Governments and industry are following closely as early policy drafts raise a number of potential concerns including their consistency with China's WTO commitments on market access. In 2003, the State Development and Reform Commission, released a draft of its new auto policy. The draft policy, demonstrates that the Chinese government is still taking a hands on approach in developing the Chinese auto industry. Concern is heightened by the apparent lack of transparency in the formulation of these policies and a failure to allow for substantive comment by WTO members and their affected firms.

Foreign Manufacturers and their Joint Venture Partners in China

- Estimated 2003 production includes passenger and commercial vehicles.
- Estimated production/estimated capacity in bold.

General Motors

- GM has invested over $US 1.58 billion in China.
- GM's joint ventures include SAIC, SAIC-Wuling, Jinbei-GM and SAIC-GM-Wuling.
- Currently, GM has 8% of the Chinese market.
- In 2002, GM sold 258,000 vehicles, an increase of 325% over 2001 sales.
- 2003 sold 335,000 units.
- GM is importing and considering assembling at least three of its Cadillac models in China.
- In 1999, it is reported that GM made over $US 72 million in profit in China.
- GM has about 9000 employees and 200 dealers in China.

Chongqing Chang'an Suzuki Automobile **92,948 /100,000**
(Chang'an Automotive Liability 51%, Suzuki 35%, Nisshio Iwai Trading 14%)
Shanghai GM Automotive Co. **175,797/300,000** by 2005
(Shanghai Automotive Industry Corp. 50%, GM 50%)
GM-Wuling Automotive Stock Ltd. **147,055/336,000** by 2006
(Shanghai Automotive Industry Corp. 50%, GM 34%, Wuling Automotive 16%)
Jinbei GM Automotive Co. **5,418/50,000**
(First Auto Works-Jinbei Automotive Corp. 50%, General Motors 50%)
Yantai GM (Formerly Daewoo) **/100,000**
(GM 25%, SAIC GM 25%, SAIC 50%)
Dongyue GM **/100,000**
Chang'an Suzuki **/100,000**
Quingling Isuzu **/100,000**

Ford

- Ford reached an agreement in October 2002 with joint venture partner Chang'an Ford, to further invest US$1.5 billion to expand the annual production of Chang'an Ford from the current 20,000 units to 150,000.
- By 2007, Ford plans to have four locally made vehicles.
- Ford employs about 6,500 in China.

Chang'an Ford Automobile Co. **23,882 /50,000** **150,000 future**
(Ford Motor Co. 50%, Chang'an Automotive Liability 50%)
Ford Jianling **/60,000**

Daimler Chrysler

- DCX Jeep unit has been building its Jeep models in China since 1983 and was China's first auto joint venture. In September 2003 DCX announced a new agreement with Beijing Jeep. The partners plan to invest 1.2 billion to modernize and expand the Beijing Jeep facilities.

Beijing Jeep Corp. **29,799 /100,000**

(Beijing Automotive Industry Corp. 58%, DaimlerChrysler AG 42%)

Mitsubishi **/300,000 by 2007**

Volkswagen

- Volkswagen/Audi has roughly 40 % of the Chinese market.
- Volkswagen sold 600,000 VWs and Audis in 2003.
- Volkswagen sells more cars in China than in Germany.
- Volkswagen has plans to invest another six billion euros to double its annual production capacity up to 1.6 million units within the next five years. Volkswagen plans to build a third factory in a joint venture with SAIC (Shanghai Automotive Industry Corp).
- Volkswagen also has a joint venture with the largest Chinese automaker FAW.
- Volkswagen plans to sell 1 million vehicles per year by 2007.

FAW-Volkswagen Automotive Co. **278,546/ 660,000 by 2007**

(First Auto Works 60%, Volkswagen AG 30%, Audi AG 10%)

Shanghai Volkswagen Automotive Co. **364,859/500,000**

(Volkswagen AG 50%, Shanghai Automotive Industry Corp. 25%, Bank of China Shanghai Trust and Consulting 15%, CNAIC 10%)

Toyota

- Toyota plans to sell 150,000 units in China by 2004.
- Toyota has plans to build 300,00-400,000 units in China by 2010

Tianjin FAW Toyota Motor Co. **52,300 /110,000 by 2005**

(Toyota Motor Corp. 50%, Tianjin Automotive Industry Corp. 50%)

Guangzhou **/50,000 by 2005, 200,000 long term**

(Toyota Motor Corp 50%, Guangzhou 50%)

FAW Tianjin Xiali **/120,000**

(Technology Licensing)

Jinbei Motors **/80,000**

(Technology Licensing)

Nissan/Renault

Dongfeng Motor Co. **325,158/550,000 by 2006, 900,000 by 2012**

Zhengzhou 70% Nissan 30% **/72,000**

Yulon 25 %, Nissan 75% **/30,000**

FAW Tianjin **102,034/120,000**

(Xiali)

Zhengzhou Nissan Automobile Co. **16,993**/

Honda

- Honda is the first foreign auto manufacturer that has announced plans to export from China.

Guangzhou Honda Automotive Co. **105,630/150,000**

(Guangzhou Automotive Group 50%, Honda Motor Co. 50%)

Dongfeng Honda **30,000 by 2004**

Honda Automobile **50,000 by 2004** (for export)

Hyundai
Beijing Hyundai Motor Co. **47,801/550,000 by 2010**
Dongfeng Yueda Kia Motor Co. **48,830 /400,000 planned**
(Kia 50%, Dongfeng Automotive Group 25%, Yueda 25%)

PSA
Dongfeng Peugeot Citroen Automotive Co **99,177 /300,000 by 2006**
(Dongfeng Motors 70%, PSA/Peugeot-Citroen 30%)

BMW
BMW Brilliance Auto Ltd. **1,293/30,000, 100,000 by 2014**
(BMW 50%, Brilliance China Automotive Holdings Ltd. 45%, Shenyang City 5%)

Fiat
Nanjing Fiat **90,000, 150,000 by 2006**

SAIC-CHERY **75,035/**

Geely Automotive **46,995/**